FOS complaints and civil proceedings

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FINANCIAL REGULATION : NEGLIGENCE : CIVIL PROCEDURE : ADMINISTRATIVE LAW

CAUSES OF ACTION : COMPENSATION : FINANCIAL ADVISERS : FINANCIAL OMBUDSMAN SERVICE : FINANCIAL SERVICES : NEGLIGENCE : RES JUDICATA : EFFECT OF AWARD UNDER FINANCIAL OMBUDSMAN SCHEME ON ABILITY TO BRING FURTHER CLAIMS : APPLICATION OF RES JUDICATA : FINANCIAL SERVICES AND MARKETS ACT 2000 s.228(5)

Summary: *The Financial Ombudsman Service (FOS) is an increasingly important means of alternative dispute resolution in respect of complaints made by consumers, micro-enterprises and small charities. The recent Court of Appeal decision in* Clark v In Focus Asset Management *provides timely clarification of a complainant's ability to bring civil proceedings having previously made a successful FOS complaint. This article also considers the relationship between the FOS jurisdiction and court proceedings in the context of applications to strike out proceedings, stays of proceedings pending resolution of a FOS complaint, and costs in civil proceedings where a party has failed to engage appropriately with the FOS process.*

Background

A comprehensive analysis of the background and case law relating to the FOS may be found in Fred Philpott's Chapter 11 of *Modern Financial Regulation,* Kirk & Ross (Jordan, 2013). The FOS jurisdiction is likely to assume increasing importance following the transfer of consumer credit regulation from the OFT to the FCA on 1 April 2014. For example, firms are now required to comply with new rule CONC 7.15.10 contained in the FCA Handbook which requires that a lender must not initiate legal proceedings in relation to a regulated credit agreement where the lender is aware that the customer has submitted a valid complaint or what appears to the firm may be a valid complaint relating to the agreement in question that is being considered by the FOS.

FOS COMPLAINTS AND CIVIL PROCEEDINGS
BY JAMES ROSS

In the recent case of *Clark v In Focus Asset Management and Tax Solutions Limited,*[1] the background to the FOS jurisdiction under the Financial Services and Markets Act 2000 (FSMA) was summarised as follows:

> '17. The Ombudsman Service was set up under the FSMA to provide consumers of financial services with an independent dispute resolution service if they had a dispute with a financial adviser regulated under that Act. It subsumed and replaced some eight ombudsmen schemes, some of which were established by self-regulatory organisations set up pursuant to the Financial Services Act 1986.
> 18. The rules governing the Ombudsman Service form part of the Handbook issued by the FCA in a section called the Dispute Resolution: Complaints Sourcebook ("DISP").
> 19. The relevant provisions of FSMA start:
> "225(1) This Part provides for a scheme under which certain disputes may be resolved quickly and with minimum formality by an independent person.
> (2) The scheme is to be administered by a body corporate ("the scheme operator)."
> 20. The scheme operator, Financial Ombudsman Service Ltd, appoints a panel of persons appearing to it to have appropriate qualifications and experience to be ombudsmen (FSMA, schedule 17 paragraph 4). (The word "ombudsman" comes from the Swedish. Modern variations include "ombud" and "ombudsperson".) An ombudsman generally handles complaints, but it is clear that FSMA extends their functions well beyond this to the speedy investigation, mediation and resolution of disputes, requiring financial advisers to take specified steps and the award of compensation. Parliament may well have chosen the term "ombudsman" because that term was used by some of the earlier schemes and because the ombudsman was to investigate matters, which a court or tribunal would rarely do.
> 21. FSMA gives the Ombudsman Service a (i) voluntary, (ii) compulsory and (iii) consumer credit jurisdiction. This appeal concerns only its compulsory jurisdiction. DISP 2.7 provides that a complainant must be an "eligible complainant" to make a complaint. DISP 2.7.3 provides that an eligible complainant must be a consumer, a micro-enterprise, a charity with an annual income of less than £1m or a trust with net assets of less than £1m. A consumer is a "natural person acting for purposes outside his trade, business or profession". A micro-enterprise is a body that has less than ten employees and a turnover or balance sheet of less than €2m. The eligible complainants other than consumers are therefore relatively speaking small entities likely to have the same knowledge or experience as consumers. In the interests of simplicity I will use the term "consumer" to cover all eligible complainants. The defendant to a complaint may be a financial adviser or a provider of financial services, such as banking, insurance or investment services, but I will for simplicity use the term "adviser" to refer to a defendant to a complaint.
> 22. A key component of the process of the Ombudsman Service is that it he gives each side the chance to put their case in writing. In some cases an adjudicator will carry out a preliminary investigation and report to the ombudsman before the ombudsman decides whether to proceed. There may or may not be a hearing in front of the ombudsman. He may direct that oral evidence

[1] [2014] EWCA Civ 118

be received and that the parties supply documents to him, but there is no cross-examination of witnesses and there is no formal disclosure of documents between the parties.

23. The ombudsman determines the complaint "by reference to what is, in the opinion of the ombudsman, fair and reasonable in all the circumstances of the case" (FSMA, section 228(2); DISP 3.6.1). He can, therefore, ignore technicalities in the law or a lack of evidence or award compensation which would not have been recovered at law if he thinks that is the right course. On the other hand he may in any particular case conclude that it would be wrong to depart from the legal position. DISP 3.6.4R fleshes out the process by requiring the ombudsman, when considering what is fair and reasonable, to take into account the law, regulatory requirements rules, codes of practice and so on.

24. The power to decide a dispute according to what is fair and reasonable is not carte blanche. As Stanley Burnton J (as he then was) held in *R(IFG) v Financial Ombudsman Service* [2006] 1 BCLC 534, [13], the court may set aside the ombudsman's decision if it is perverse or irrational.

25. At the end of the process the ombudsman issues an award. Section 229 expressly gives the ombudsman the power to award "compensation". The compensation may not exceed the limit specified by rules made (now) by the FCA "but the ombudsman may, if he considers that fair compensation requires payment of a larger amount, recommend that the respondent pay the complainant the balance" (section 229(5)).

26. An award that involves the payment of a sum of money can be enforced as a county court judgment (section 229(8)(b), schedule 17, paragraph 16). So a money award, if accepted, leads to the creation of a legal right, namely the right to receive the sum awarded and this right is enforceable as if it were a judgment of the court.

27. A defining feature of the Ombudsman Service is that a complainant can choose not only whether to submit his complaint to it in the first place but also whether to accept the decision of the Ombudsman, but if he accepts the determination within the time limit, it is final and binding on both parties. This follows from section 228, which provides:

"(5) If the complainant notifies the ombudsman that he accepts the determination, it is binding on the respondent and the complainant and final.

(6) If, by the specified date, the complainant has not notified the ombudsman of his acceptance or rejection of the determination he is to be treated as having rejected it.

(6A) But the complainant is not to be treated as having rejected the determination by virtue of subsection (6) if—

(a) the complainant notifies the ombudsman after the specified date of the complainant's acceptance of the determination,

(b) the complainant has not previously notified the ombudsman of the complainant's rejection of the determination, and

(c) the ombudsman is satisfied that such conditions as may be prescribed by rules made by the scheme operator for the purposes of this section are satisfied…."

28. The ombudsman may award the complainant his costs, but he cannot make any order for costs against the complainant (section 230).'

The FOS annual report for the financial year 2012-2013 shows how important the FOS has become in resolving disputes relating to retail banking and financial services:

> 'We handled 2,161,439 initial enquiries and complaints from consumers – over 7,000 each working day.
>
> Around 1 in 4 of the initial consumer enquiries we received turned into a formal dispute – a record 508,881 new cases, up 92% on the previous year.
>
> 74% of new cases were about the sale of payment protection insurance (PPI), with the number of PPI complaints rising 140% to 378,699.
>
> Investment-related complaints increased by 33%, while banking disputes and complaints about insurance other than PPI rose by 20% – resulting in the highest ever numbers of these cases.'

Res judicata and merger in the context of FOS complaints

In *Clark v In Focus Asset Management and Tax Solutions Limited,* the Clarks' case was that they lost more than £300,000 through negligent investment advice given by In Focus Asset Management Limited, their former financial adviser. The Clarks took their complaint to the FOS, who decided that they were entitled to compensation exceeding the limit of £100,000[2] that the FOS could award. In addition to awarding the Clarks £100,000, the FOS recommended payment of full compensation. The Clarks accepted the award subject to their right to claim more in court proceedings. The firm paid the Clarks the sum of £100,000 but did not pay the full recommended amount.

The Clarks then brought High Court proceedings, which were transferred to the Chichester County Court, for damages for breach of contract, negligence, breach of fiduciary duty and breach of statutory duty, stating that they would give credit for the sum already awarded. The firm asked the court to make an order dismissing the claim. HHJ Barratt QC held that the doctrine of merger applied and made such an order. He applied an earlier High Court decision of HHJ Pelling QC, sitting as a deputy judge of the High Court of Justice, Chancery Division, in *Andrews v SBJ Benefit Consultants* [2011] PNLR 577. However, on appeal, Cranston J held that the Clarks' causes of action did not merge in the FOS award. He disagreed with the decision in *Andrews*. Accordingly he concluded that HHJ Barratt QC had been wrong to dismiss the proceedings. The Clarks appealed from the order made by Cranston J and the Court of Appeal was therefore required to resolve the conflicting High Court decisions.

When giving judgment in the *Clark* case, Arden LJ summarised the principles of res judicata and merger as follows:

[2] The limit increased to £150,000 with effect from 1 January 2012.

'3. Common law doctrines preclude a person who has obtained a decision from one court or tribunal from bringing a claim before another court or tribunal for the same complaint. These rules are referred to as res judicata and merger. The parties have argued this case on the basis of both principles. The judge dealt solely with merger.

4. To understand merger, it is necessary to understand the meaning of "a cause of action". It is not a legal construct. The term "cause of action" is used to "describe the various categories of factual situations which entitle[d] one person to obtain from the court a remedy against another" (per Diplock LJ in *Letang v Cooper* [1965] 1 QB 232 at 242. A complaint to the ombudsman need not be a cause of action but (as further discussed below) it may involve consideration of an underlying cause of action and the facts on which a complaint is based may be or include facts constituting a cause of action.

5. Merger explains what happens to a cause of action when a court or tribunal gives judgment. If a court or tribunal gives judgment on a cause of action, it is extinguished. The claimant, if successful, is then able to enforce the judgment, but only the judgment. The effect of merger is that a claimant cannot bring a second set of proceedings to enforce his cause of action even if the first tribunal awarded him less than he was entitled to (see, for example, *Wright v London General Omnibus Co* [1877] 2 QBD 271 and *Republic of India v Indian Steamship Company Ltd (The Indian Grace)* [1998] AC 878). As Mummery LJ held in *Fraser v HMLAD* [2006] EWCA Civ 738 at [29], a single cause of action cannot be split into two causes of action.

6. Res judicata principally means that a court or tribunal has already adjudicated on the matter and precludes a party from bringing another set of proceedings (see generally *Lemas v Williams* [2013] EWCA Civ 1433). The doctrine also covers abuse by a litigant of the court's process by bringing a second set of proceedings to pursue new claims which the claimant ought to have brought in the first set of proceedings (this is known as the rule in *Henderson v Henderson* (1843) 3 Hare 180; 67 ER 313).

7. The requirements of res judicata are different from those of merger. All that is necessary to bring merger into operation is that there should be a judgment on a cause of action. Res judicata may apply either because an issue has already been decided or because a cause of action has already been decided. We are concerned on this appeal with res judicata of the latter kind, known as cause of action estoppel.

8. I take as the requirements of cause of action estoppel the summary from Spencer Bower and Handley on Res Judicata cited with approval by Lord Clarke (with whom Lords Phillips, Rodger and Collins agreed) in the recent case of *R(o/a Coke-Wallis) v Institute of Chartered Accountants in England and Wales [2011]* 2AC146 at [34]:

"34 In para 1.02 Spencer Bower & Handley, Res judicata, 4th ed makes it clear that there are a number of constituent elements in a case based on cause of action estoppel. They are:

"(i) the decision, whether domestic or foreign, was judicial in the relevant sense; (ii) it was in fact pronounced; (iii) the tribunal had jurisdiction over the parties and the subject matter; (iv) the decision was— (a) final; (b) on the merits; (v) it determined a question raised in the later litigation; and (vi) the parties are the same or their privies, or the earlier decision was in rem."

9. If the requirements of res judicata are fulfilled, they constitute an absolute bar and the court has no discretion to hold that res judicata should not apply in any particular case.

> 10. If the requirements of merger are satisfied, it is unnecessary to see if the requirements of res judicata were fulfilled, and vice-versa.
> 11. There is a powerful two-fold rationale for the doctrines of merger and res judicata. The first rationale is "the public interest in finality of litigation rather than the achievement of justice as between the individual litigants" (see per Lord Goff in *The Indian Grace* at 415). Mr Clive Wolman, for the respondents, suggests that the public interest in finality arises out of a concern that the public courts and tribunals should not be clogged by repetitious re-hearings and re-determinations of the same disputes. This is clearly a powerful consideration.
> 12. Second there is the private interest. As Sir Nicolas Browne-Wilkinson V-C put it in *Arnold v National Westminster Bank plc* [1983] 3 All ER 977 at 982: "it is unjust for a man to be vexed twice with litigation on the same subject matter".'

The Court of Appeal concluded that, having accepted the FOS award, the Clarks were not entitled to bring subsequent court proceedings for two reasons: firstly, apart from the FSMA, the common law doctrine of res judicata applied to FOS adjudications; and secondly, there was nothing in the FSMA which precluded the application of the doctrine of res judicata.[3] Given that the requirements of res judicata were satisfied, it was unnecessary to determine whether the requirements of merger were fulfilled.[4]

This is a clear decision which brings welcome clarity to this area. Nevertheless, a few residual questions remain as to the application of this ruling in future cases. This is because the factual matrix on which a complaint is based may differ to a greater or lesser extent from those facts relied upon in subsequent court proceedings. FOS complaints are often somewhat ill-defined in terms of their scope, especially where the complainant is not legally represented. In order to apply the decision in *Clark* when striking out a claim following a FOS complaint, the court will need to consider whether the subject matter of the claim is sufficiently similar to that of the complaint that the principle of res judicata applies. Further, even where the subject matter of the complaint and the claim are different, the firm could maintain an argument based on *Henderson v Henderson* abuse that the consumer could and should have raised all issues when making the complaint. However, the cases in which a *Henderson v Henderson* argument will be successful are likely to be fairly rare: the Court of Appeal in *Clark* was careful to point out that under that rule, fresh proceedings are not automatically precluded and the court has to reach a "broad merits-based judgment" as to whether the court proceedings are abusive. Different factors might

[3] See paragraph 2 of the judgment.

[4] See paragraph 10 of the judgment.

therefore arise and "one can expect a court to scrutinise very closely indeed (by reference to the facts of the case) any application for a stay of the legal proceedings on such a basis".[5]

Situations where the FOS award or offer of redress is rejected by consumer

In the *Clark* case, the FOS made the maximum possible award and the Clarks, ultimately unsuccessfully, sought to recover by court proceedings the additional sums which they said represented their true loss. This scenario is relatively rare: the FOS intervened in the appeal to the Court of Appeal and submitted evidence that there were around 87 such maximum awards made by FOS in a calendar year,[6] which is a relatively trivial number when compared with the total number of complaints and enquiries exceeding 2 million received by FOS in the financial year 2012-2013. Nevertheless, the principle in *Clark* will apply equally where the FOS makes an award which is less than the current £150,000 maximum but where the complainant feels that his losses exceed the amount of the award. Following *Clark*, if a complainant in such a situation accepts the FOS award, he cannot then bring court proceedings relating to the same subject matter in order to recover the rest of his perceived losses.

What of the situation where the consumer rejects the FOS award and decides to issue proceedings? As set out above, the consumer has the right to reject the FOS determination under section 228 of the FSMA and in those circumstances the firm will not usually be able to prevent the consumer from taking the matter to court. However, this is subject to two important caveats: the court may stay proceedings if they serve no legitimate purpose and failure of the consumer to accept the FOS award or otherwise engage in the FOS process may have a later adverse impact in costs.

An example of the first circumstance may be seen in the case of *Binns v FirstPlus Financial Group plc* [2013] EWHC 2436 (QB).[7] In the *Binns* case, the complaint relating to PPI mis-selling never reached the FOS because an offer of full redress was made by the firm under the DISP rules as its first response to the written complaint. However, the consumer's solicitors, Wixted & Co, indicated that settlement would not be agreed unless provision was made for their costs. No such provision was forthcoming and a claim was subsequently issued which was materially identical to the complaint which the firm had offered to settle in full. A District Judge dismissed

[5] Per Davis LJ at [129].

[6] See paragraph 38 of the judgment.

[7] Notwithstanding the High Court neutral citation, it is not entirely clear whether HHJ Jeremy Richardson QC was sitting as a High Court judge for the purpose of hearing the appeal.

the firm's application for summary judgment but granted permission to appeal. On appeal, HHJ Jeremy Richardson QC summarised his conclusions as follows at [43]:

> "43. In my judgment the moral of this case is that litigants should ordinarily follow the ADR route when there is a perfectly good scheme that offers (i) speedy justice; and (ii) full redress. In appropriate cases the court should and will strike out cases where there has been full redress already. Full redress relates to matters intrinsic to the case not costs adjunctive to it. Using the language of CPR Part 3.4 (2)(a) there is truly no reasonable ground for bringing the claim. How can it be reasonable to bring a claim when the claim has succeeded in every way via ADR? The court needs to encourage good ADR and not allow claims that have succeeded to carry on. I dare say this case will be fact specific to the PPI litigation, but there may be wider applicability to other forms of ADR. I do not see a potential costs advantage as being a legitimate reason to press on with a case of this kind. The mosaic presented to me in this case admits, in my judgment, of one answer – strike-out."

The judge was careful to note the critical point that the firm's offer of redress remained open for acceptance and this was recorded in the order dismissing the claim. It is respectfully submitted that the reasoning in this case was sound and should apply equally where the firm offers redress under the DISP rules as well as where the FOS has made a final determination which remains capable of acceptance. Where the claimant has already been offered full redress and the offer remains open, the claimant should not be permitted to pursue legal proceedings merely in order to generate and recover costs: there is no legal entitlement to recover costs incurred at the early stages of a dispute which is settled pre-action (see *McGlinn v Waltham Contractors Limited* [2006] 1 Costs LR 27). This is a merely an application of the general rule that it is an abuse of process to issue proceedings where the benefit attainable by the claimant in the action is of such limited value that "the game is not worth the candle" and the costs of the litigation will be out of all proportion to the benefit to be achieved (see *Jameel v Dow Jones and Co* [2005] QB 946). It is inappropriate for parties seeking to resolve a dispute between them as to costs to seek to do so by litigating to a conclusion a substantive issue that has become academic (see *R (Tshikangu) v Newham LBC* [2001] EWHC Admin 92).

Costs consequences where a consumer fails to engage with the FOS process

The Jackson reforms to the Civil Procedure Rules implemented in April 2013 place particular emphasis on the need to manage costs and manage cases proportionately. At the pre-action stage, in paragraph 6.1 of the Practice Direction on Pre-Action Conduct, it is provided that:

> "Before starting proceedings, the parties shall make appropriate attempts to resolve the matter without starting proceedings and in particular consider the use of an appropriate form of ADR in order to do so."

The commentary at C1A-007 of volume 1 of the White Book complements this by stating under "Considering alternatives to litigation":

> '…parties and their advisers need to consider whether any of the following might be appropriate…. making a formal complaint to the organisation in question or at the next stage, a complaint to the Ombudsman.'

In *Andrew v Barclays Bank plc* [2012] EWHC B13 (Mercantile), HHJ Waksman QC (sitting as a judge of the High Court) gave the following general guidance in relation to the interaction between resolving disputes under the DISP scheme and court proceedings at [39]:

1) A person who considers he may have a PPI mis-selling claim should first make a complaint under the DISP scheme.

2) If the complaint is not resolved, a letter before claim should be sent.

3) If a claimant issues proceedings without making a complaint under the DISP scheme, he is at risk of the matter being stayed to be considered under DISP and being ordered to pay the costs of any application for such a stay.

The judge also found that PPI disputes were clearly suitable for resolution by the FOS and warned that '*a person with a PPI claim who hereafter fails to engage with the Scheme but instead proceeds straight to litigation must at least be at a real risk of an adverse costs order even if successful in the claim at the end of the day*'.[8] This warning applies with all the more force following the recent decision of the Court of Appeal in *PGF II SA v OMFS Company 1 Limited* [2013] EWCA Civ 1288, where it was held that a party's silence in response to an invitation to engage in ADR could itself be considered as unreasonable and would likely result in an adverse ruling on costs.

[8] See paragraph 27 of the judgment.

Summary

The relationship between the FOS jurisdiction and civil proceedings may be summarised by the following principles:

1) A consumer who considers he may have a claim against a firm should first make a complaint under the DISP scheme.[9]

2) Where a consumer accepts an award following a final FOS determination, he cannot then bring civil proceedings based on the same subject matter.[10]

3) A consumer has the right to reject a FOS determination under section 228 of the FSMA but where full substantive redress is already available to the consumer under the DISP scheme, there is a risk that a subsequent claim will be struck out.[11]

4) If a claimant issues proceedings without making a complaint under the DISP scheme, he is at risk of the matter being stayed to be considered under DISP and being ordered to pay the costs of any application for such a stay.[12]

5) Where a consumer fails to make a FOS complaint or otherwise engage with the DISP process, he is at serious risk of costs sanctions even if he is ultimately successful on his claim.[13]

[9] See paragraph 6.1 of the Practice Direction on Pre-Action Conduct and *Andrews v Barclays Bank plc* (above) at [39].

[10] See the *Clark* case above.

[11] See the *Binns* case above.

[12] See the *Andrews* case above.

[13] See the *Andrews* case above at [27] and the *PGF* case more generally.